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THE 1949 STERLING CRISIS AND BRITISH
POLICY TOWARDS EUROPEAN INTEGRATION

by

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The 1949 Sterling Crisis and British Policy towards European Integration

A conventional wisdom prevails in the histories of postwar European integration. The late Jean Monnet, high priest of the European Movement, and his acolyte Richard Mayne, have been joined by various European and American scholars in the propagation of a persuasive historical orthodoxy.¹ There are three assumptions fundamental to this orthodoxy. First, the Marshall Plan not only saved Western Europe from political and economic ruin after 1947 by helping it to overcome the dollar shortage, but created the conditions for international economic expansion. Secondly, the Marshall Plan gave material and institutional form to the 'European Idea' and established the foundations of the European Community by providing participating countries with hard currency and by encouraging mutual aid on the continent through the O.E.E.C. Thirdly, the British ultimately kept aloof from the new Europe because of an anachronistic determination to play a world role, albeit at the centre of a multiracial Commonwealth rather than at the heart of an Empire.

This paper challenges those assumptions. In particular it challenges the assumptions about British policy towards Europe after 1947. It is true that (after 1947) the British did place the maintenance of their world role at the centre of the sterling area above any irreversible commitment to European integration. But that decision was not founded upon political arrogance. London believed that Europe's dollar problem was part of a much wider international disequilibrium the solution of which was dependent on sterling-dollar co-operation. A study of the 1949 sterling crisis both explains the economic rationality

of the British approach and suggests that the Marshall Plan failed to bridge Europe's dollar gap.

I

American policy-makers in the State Department launched the Marshall Plan in the belief that Europe's postwar dollar shortage threatened all the plans made during the Second World War for the construction of an open world economy. Their anxiety was that without a continuing flow of hard currency from the United States, European nations would increasingly turn to bilateralism, State trading and exchange controls to eliminate the dollar from intra-European trade. If the non-Soviet world, and with it the American economy, were to be kept safe for free enterprise, Europe's commitment to liberal capitalism had to be guaranteed.

This commitment was to be secured by the transformation of Western Europe into an integrated economic community in which participating countries would encourage mutual aid, self-help and the free flow of men, goods and capital. The hope in Washington was that the Marshall Plan, or European Recovery Programme (E.R.P.), would correct the imbalance between Europe and the Western Hemisphere by stimulating production in participating countries on the basis of large dollar grants and the liberalisation of trade barriers and exchange controls. Further, balance between Europe and the dollar area was to be the first step on the road to world-wide convertibility and multilateralism. Robert Triffin later emphasised that Washington hoped to build

a large and stable area of free trade, gradually drawing non member countries into its orbit.⁽²⁾

American officials envisaged a new international system in which Western Europe would become the United States' junior partner both in the achievement of multilateralism and, of course, in the containment of perceived Soviet expansion.

The Marshall Plan rested on two basic assumptions. The first was, as Will Clayton told members of the British Cabinet in the summer of 1947, that the dollar shortage "represented (the) failure of Europe to produce".⁽³⁾ The second was that Britain should lead the process of West European integration. American policy-makers felt that the events of 1947 - the fuel crisis, the withdrawal from Greece and Turkey and the convertibility crisis - had shown that the United Kingdom's days as a world power were past. Yet no other West European Country possessed Britain's stability and political influence. The British should therefore substitute leadership in Europe for their world role.

The British shared neither of these assumptions. First, they argued that the dollar shortage was rooted in the collapse of the old triangular pattern of international settlements as a result of the war. The United States was in 1945 the world's greatest supplier of manufactures and capital goods. Western Europe, Britain and Japan were heavily dependent on the United States for the equipment which would allow their industries to operate and for the consumer goods which would provide their populations with a reasonable standard of living. But since

the war had reduced the immediate dollar earning capacity of far Eastern countries⁽⁴⁾ neither Britain nor the nations of Continental Europe were now able to finance their dollar deficits with offsetting surpluses. The British maintained that only a return to triangular trade could lead to a lasting solution of the disequilibrium. Merely increasing European production without simultaneously replenishing the hard currency stocks of the underdeveloped and developing countries of the far East was an inadequate and misconceived policy.

Secondly, from the moment the Marshall Plan was launched the British struggled against American attempts to confine them to a European role. London argued that Britain's position at the centre of the sterling area inevitably gave her a world role the maintenance of which was essential to the world economy in general and to the British economy in particular. As the gold and dollar reserves drained away during the 1947 convertibility crisis the sterling area had come near to disintegration. Studies in the British Treasury at the same time had concluded that the collapse of the sterling area would precipitate a global liquidity crisis and lead to mass unemployment in the United Kingdom.⁽⁵⁾

The 1945-51 Labour Government became convinced after the convertibility crisis that the preservation of sterling area viability had to be the basis of any initiative designed to overcome the dollar shortage. Traditionally Britain had been at the centre of the world economy, financing deficits with the West by surpluses with the East. The United States should not, therefore, treat Britain simply as part of the European breadline. Rather, Washington should be prepared to make special arrangements for Britain which, in leading to an expansion of sterling area reserves, would put hard currency into the hands of Empire and

Commonwealth nations, many of which were primary producers. The return to triangular trade was to be stimulated by an Anglo-American financial partnership. By acting as the world's creditor along the lines suggested by Keynes in 1943 and 1944 the United States could correct the disequilibrium, so helping to shape with Britain an expansionary international economic environment in which the Attlee Government's liberal socialism could flourish.

American support for sterling area reserves was not forthcoming. Indeed, after 1947 Anglo-American economic relations were marked by friction as members of the State Department and the Economic Co-operation Administration (E.C.A.) became increasingly frustrated at Britain's unwillingness to inaugurate bold moves to European integration. The British shared the American anxiety about Soviet expansion and agreed that West European nations should co-operate to offset the power of the Soviet bloc in Eastern Europe. But the United Kingdom believed that membership of a closely-knit European community would threaten the viability of the sterling area. Since the sterling area was in deficit with Belgium and to a less extent with Switzerland the area reserves stood to lose large amounts of hard currency in any sweeping liberalisation of European exchanges. Britain therefore countered American and continental pressure for integration by sponsoring through the O.E.E.C.⁽⁶⁾ an intergovernmental form of West European association which would enable her to reconcile her world economic role and her commitment to domestic full employment with the imperative of European co-operation. The British maintained that they would be able to take more chances in Europe if the Americans gave some financial ballast to the world's second international reserve currency. But until Britain could free herself from

anxiety about the level of the sterling area reserves she would have to keep intact the rigorous system of exchange controls introduced after the suspension of convertibility in August 1947. In Washington these British arguments were regarded as pleas for the support both of doctrinaire socialism and of economic discrimination. The concessions won for sterling in the European payments scheme negotiated in 1948 derived not from American acceptance of international Keynesianism but from British success in persuading the United States of the sterling area's value to European countries seeking non-dollar sources of supply.⁽⁷⁾ These related disagreements about the adequacy of the Marshall Plan in countering the dollar shortage, Britain's determination to protect the sterling area and attitude to European integration finally came to a head during the 1949 sterling crisis.

II

The events of 1949 were to belie the American view that the main cause of the dollar shortage was Europe's failure to produce and justify the British views of the problems facing the world economy. The E.C.A. Recovery Guides published in June 1949 noted that

(West European) Production is flowing at an increasingly rapid rate - bottlenecks to industrial expansion have almost everywhere disappeared, inflationary pressures have abated ... The European economy seems to be entering a more critical phase of development - a phase in which the problems of markets, trade, prices, distribution and economic balance take the place of production, allocation and rationing. The O.E.E.C. countries are thus required, perhaps sooner than anticipated to adjust their economies internally, between each other, and the rest of the world, particularly with the 'hard currency' areas. (8)

In other words, despite their steady success in maintaining economic recovery, participating countries had not made great strides towards a solution of the dollar gap. Western Europe's industrial output for the second quarter of 1949 reached its highest point since the war, 117 per cent of the level attained in 1938. Yet the overall trade deficit of participating countries increased. In the fourth quarter of 1948 the deficit was \$1.2 billion; for the first quarter of 1949 it stood at \$1.6 billion. Of the second quarter deficit \$1.0 billion was with the United States.

Opportunities for increased dollar earnings were reduced in the first half of 1949 by a recession in the United States which had started in the latter part of 1948. It has been estimated that the rate of growth of consumption in the United States dropped by 6 per cent in 1948.⁽⁹⁾ This levelling of consumer demand precipitated a contraction in the United States economy for a period of 11 months, from November 1948 to October 1949. Industrial production dropped by 10 per cent, while there was a decline of slightly more than 5 per cent in the G.N.P.⁽¹⁰⁾

Although the American recession was mild compared with either that of 1929 or 1938 its results both for Marshall Europe and for the rest of the world were serious. The fall in American prices enabled European countries to import a higher volume of goods with the dollars they possessed while making European exports throughout North and South America less competitive than goods produced in the United States. In 1948 Europe had imported goods to the value of \$4,340 billion from the United States. In the first half of 1949 the value of European imports from the United States stood at an annual rate of \$4,703 billion.⁽¹¹⁾ The buoyancy of imports from, and the fall in exports to, the dollar area (Europe's share of the United States market fell from 15.4 per cent in 1948 to 12.6 per cent by the end of June 1949) put an increasing strain on the reserves of European countries.

The result of Europe's failure in hard currency markets in 1949 was the reinforcement of the traditional links maintained by participating countries with their overseas dependence and with independent sterling area countries. Exports whose prices were too high for the American market were switched to soft

currency areas. There was, then, no decline in the level of exports from Western Europe in the first half of 1949. Indeed by comparison with the second quarter of 1948 exports rose by \$400 million and by \$190 million and \$290 million to overseas dependencies and participating countries respectively. Noting this development the September 1949 Recovery Guides spoke of a trend towards the compartmentalisation of the Western world's economy into separate trading areas. (12)

The part played by traditional links between a Metropolitan country and its currency area in increasing the flow of exports can be understood best by an examination of the sterling area. No formal exchange controls operated within the area. There was a steady outflow of capital from the United Kingdom to overseas members of the area throughout the postwar years. Between 1946 and 1949 these capital exports totalled £703 million. (13) Demand for British goods within the sterling area therefore remained high and was fuelled by the existence of the sterling balances, which on 31 December 1948 totalled £3,554 million. (14) When a buyer's market began to replace a seller's market throughout the Western Hemisphere, therefore, the United Kingdom was able to shelter behind the sterling area and maintain expanding exports and full employment. France, Belgium and the Netherlands, also at the centre of currency areas, repeated this pattern. In 1948 supplies from European countries occupied 75 per cent of all exports to overseas dependencies: in the first half of 1949 the European share increased to 79 per cent. (15)

This trend towards compartmentalization was encouraged as the American recession made it difficult for raw material producers in the Far East to earn dollars. By the third quarter of 1949, for example, American imports of rubber had

fallen about 35 per cent below their level in 1948. The lack of demand pushed down the price of rubber in New York from 22 cents a pound to 16½ cents, while the volume was 25 per cent below the 1948 average. Malaya, a member of the sterling area, suffered most from the cut in American rubber imports and sent to the United States in 1949 only one-half of the volume of rubber it had supplied in 1948. Malaya's quarterly dollar earnings from the export of rubber in 1948 had averaged about \$45 million. For the first three quarters of 1949 the figures were respectively \$39.7 million, \$27.4 million and \$20.4 million.⁽¹⁶⁾ Throughout the sterling area producers of raw materials and manufactured goods encountered similar problems. Dollar earnings in the overseas sterling area declined by 21 per cent in the second quarter of 1949 and by 41 per cent in the third quarter. As the amount of hard currency flowing into the central reserves declined so member countries were forced to reduce their imports from the dollar area, by 25 per cent, in July 1949.

By the spring of 1949 it was clear that Europe's achievement of dollar viability by 1952 was in jeopardy. Indeed, the recession only highlighted the central weakness of the Marshall Plan: the assumption that with higher production Europe would be able to balance its trade with the United States. At the best of times European exports to the United States would tend to be uncompetitive because of the great strides in productivity made by American industry during the war. The recession *verschlimmerte* exacerbated this structural problem facing European governments and businessmen. Given the absence of any mechanism to pump dollars into the Far East it was not surprising that higher European production tended to result in the reverse of multilateralism. There was a danger

that outside Eastern Europe at least two and possibly three trading areas might develop: a dollar bloc centred on the United States, and a sterling bloc centred on the United Kingdom, while it was uncertain whether continental Europe would become part of the sterling bloc or form its own self-sufficient unit.

III

The trend towards the establishment of separate trading areas sent a frisson through the American establishment. On 17 March 1949 Paul Hoffman, E.C.A. Administrator, told Averell Harriman, the Special Representative in Paris, that the expansion of European exports to soft currency areas underscored the fact that European currencies were overvalued vis à vis the dollar. Hoffman argued that

Such overvaluation provides incentives that work against basic E.C.A. objectives. Imports from the dollar area are made cheap and European exports to soft currency areas tend to yield higher local currency prices than exports to dollar area. (17)

Hoffman recorded that discrimination against American businessmen by European countries, stemming from the fall in dollar revenues, was causing political problems in the United States. (18) The remedy lay in a general devaluation of European currencies to bring European prices in line with American. Exports to the Western Hemisphere would expand, discriminatory practices cease and the trend to soft currency blocs would be reversed.

A consensus developed between the State Department, the U.S. Treasury and E.C.A. that sterling was the key to the necessary adjustment in European exchange rates. (19) First, about 50 per cent of the world's visible and invisible trade was conducted in sterling; and secondly, most Marshall countries would tend to follow sterling to avoid being undercut in home and overseas markets.

American attempts to hustle the I.M.F. into calling for a review of European exchange rates in the spring of 1949 were beaten off by the British, who viewed the prospect with alarm.⁽²⁰⁾ The passage of a resolution in the Fund which accounted to a call for the devaluation of sterling would not remain secret for long. Sterling would begin to look a poor investment. Importers wishing to purchase sterling area products would hold off in the expectation of concluding a better deal. British foreign trade would suffer and export earnings sag.

Although the United States became more discrete in its calls for a review of European exchange rates it had a second string to its bow in the drive to reduce the difference in costs and prices between participating countries and the Western Hemisphere. This second string took the form of an attempt to improve Marshall Europe's competitiveness by liberalising the intra-European payments arrangements made in 1948. Bilateral drawing rights should be replaced either by convertible or by transferable drawing rights so that participating countries could purchase goods in the cheapest markets. British producers in particular would then be subject to genuine competition in Europe and would be forced to adjust costs and prices. If drawing rights were convertible participating countries could use them to finance dollar imports, leaving European producers competing not just with each other but also with American businessmen. The forced re-entry of the dollar into intra-European trade through a revised payments scheme would be both a spur to efficiency and a decisive move in the direction of an open world economy.

Proposals for convertible drawing rights were effectively blocked by participating countries, the British leading the way.

There was a general anxiety that convertible drawing rights would stimulate a competitive scramble for hard currency in Marshall Europe.⁽²¹⁾ O.E.E.C. nations would reduce imports on intra-European account to save currency to finance dollar supplies. American businessmen might find outlets but commerce among O.E.E.C. members would fall into a downward spiral at a time when unemployment stood at 1 million in West Germany, at almost 10 per cent in Belgium and when deflation in Italy was sharp enough to cause even E.C.A. concern.⁽²²⁾

E.C.A. thus withdrew its proposals for convertibility. But pressure for transferable drawing rights was maintained. The Americans were supported by Belgium and Switzerland, both all-round creditors in Marshall Europe. Under existing bilateral agreements both countries stood to gain dollars from the transfer of other European currencies to their accounts. Once again, however, the British fought against the plan. The proposals came at a bad time for London. British exports to the United States fell throughout the spring and sterling area sales slumped as a result of the American recession. The strain on the reserves was intensified by heavy transfers of gold to Switzerland and Belgium, totalling £22.4 million, arising from the first Intra-European Payments Scheme. By the end of June 1949 the British reserves had fallen to £406.4 million with the downward trend likely to continue in the absence of any upturn in the American economy.⁽²³⁾

Transferability would place further pressure on the reserves since Belgium and Switzerland could pile up sterling beyond the gold points in their bilateral arrangements with Britain.

A stalemate which might have prejudiced Congressional support for continued Marshall aid was only averted by E.C.A. pressure on the O.E.E.C. and by a compromise, favourable to Britain, drawn up by Robert Marjolin. British drawing rights on Belgium were increased from \$30 million to \$85 million. It was further agreed that in the new payments scheme only 25 per cent of all drawing rights would be transferable.

These new intra-European payments arrangements were far removed from the original E.C.A. proposals. The new scheme would ensure some flexibility between participating countries but American attempts to force a readjustment of European costs and prices had been largely thwarted by Britain's determination to protect her reserves. The anti-climactic result of America's crusade for liberalisation suggested that a solution to the rapidly developing sterling area dollar crisis was a prerequisite for progress towards multilateralism. (24)

IV

On the basis of discrimination against the dollar, a domestic full employment policy and American assistance through Marshall aid, Britain had achieved striking successes in economic policy by 1949. Whereas the volume of exports in 1945 had been 50 per cent below the level reached in 1938 it stood 55 per cent higher in 1949, financing 85 per cent of Britain's imports as opposed to 33 per cent. No other country in Marshall Europe could match this record; and not even the Americans had increased output per man-hour as rapidly since the war as had the British.⁽²⁵⁾ But the sterling crisis of summer 1949 threatened to undermine British reconstruction. By 16 June Britain's dollar drain was running at an annual rate of £600 million.⁽²⁶⁾ With the reserves facing exhaustion by the end of the year the Cabinet was forced into a major reconsideration of policy.

The options facing the Labour Government were presented by Chancellor Sir Stafford Cripps to the Cabinet's Economic Policy Committee on 7 July. Cripps stated that

the policy of trying to compromise between tying ourselves to the United States economy on the one hand and, on the other, keeping ourselves insulated from it by bilateral agreements and other means, had proved to be ineffective in protecting us from the effect of change in the American level of demand. We must contemplate similar fluctuations in the American economy in the future and should have to decide whether, in spite of these fluctuations, we should try to find some long-term basis on which we should try to associate ourselves with it, or whether we should try to isolate the sterling area from it and preserve stability within that area.⁽²⁷⁾

These two options were called respectively a 'one-world' and a 'two-world' policy. A 'one-world' policy involved rapid movement towards convertibility and multilateralism and the dismantling of trade and exchange controls. A 'two-world' policy involved the construction of a fortress sterling area on the basis of bilateral trade and payments agreements abroad and at home a direction of labour, price controls and extensions of rationing. It implied, therefore, the division of the non-communist world into two major trading blocs based on the two principal international reserve currencies. Whereas a 'two-world' approach might preserve a high level of employment at the expense of living standards a 'one-world' approach would risk exposing Britain to the full impact of cyclical recessions in the American economy whilst preserving

the essential political and strategic requirements of this country as represented by the North Atlantic Pact, Western Union and Commonwealth solidarity.⁽²⁸⁾

The British decided not to attempt the creation of an insulated sterling bloc but to work towards a 'one-world' economy. This was partly to preserve the emerging postwar Atlantic Alliance. But it was also felt that under certain conditions a 'one-world' policy need not involve any sacrifice of the Government's domestic and international economic objectives. These conditions centred on America's willingness to be a 'good creditor'. Being a good creditor meant fighting the dollar shortage through commitments to the preservation of high levels of internal demand, increased foreign investment and discussions with Britain on joint Anglo-American funding of the sterling balances.

When Cripps put the essentials of the British plan for an expansionary 'one-world' economy to American Treasury Secretary John Snyder during informal talks at the start of July he did not meet with warm approval.⁽²⁹⁾ Snyder was more concerned with the steady pressure of rising costs in the British economy, making exports, he claimed, uncompetitive in hard currency markets. Overheating in the British economy was in the American view the central factor in the sterling area's growing isolation from the world economy.⁽³⁰⁾ For the Americans, this growing isolation was exemplified in the \$700 million cuts in Western Hemisphere imports agreed in July by the Commonwealth Finance Ministers.

Snyder's visceral American distrust for socialism led him to ignore the successful record of the British export drive. He showed no sign of accepting that the American recession might have much to do with British difficulties. At the same time, however, there was evidence that British goods were overpriced. At the meeting of Commonwealth finance Ministers Edgar Whitehead of Southern Rhodesia produced figures showing the relative values of British and American exports. Whitehead's statistics revealed the British products were becoming dangerously uncompetitive.⁽³¹⁾

The failure of the Cripps-Snyder talks did not discourage the Labour Government in its search for a world economy which reconciled full employment with multilateralism. A 'one-world' economy, indeed, squared with the fundamental liberalism of the Attlee Government. Confronted by Whitehead's evidence the Cabinet decided to devalue the pound in the hope that the subsequent readjustment of British prices would induce the United States to play its part as the world's creditor. At a Cabinet discussion on 28 July it was suggested that "it might prove impossible" to gain American

co-operation in establishing a satisfactory and enduring relation between the sterling and dollar worlds unless some concession could be made to their point of view. (32)

In any case, with the reserves falling below £370 million by the end of July, devaluation had become economically as well as politically inescapable. The reserves were so low by July and August that even the taking of the 'one-world' option would provide no alternative to large-scale unemployment. The sterling devaluation was to be large, of 30 per cent, from £1 = \$4.03 to £1 = \$2.80 in the hope that it would be final.

V

Cripps and Foreign Secretary Ernest Bevin embarked for Washington, for further talks on the dollar problem, in September 1949. They took with them not just the commitment to devalue but ^{Versprechen} pledges to review public spending and improve industrial efficiency. When the British revealed this package to the Americans they met with a favourable response. The Truman Administration, worried by rising unemployment, had already determined to expand the economy. (33) On hearing of the British plans American officials agreed to resume raw material stockpiling, reduce tariffs and increase foreign investment in addition to maintaining a high level of internal demand. Further, a special organisation was to be established for the continuous discussion and review of economic problems common to the United States, Britain and Canada. Sir Oliver Franks, British Ambassador in Washington, cabled that "a real conviction" had arisen from the talks that the countries represented there

have it in their power to remake the economic and trade pattern of the Western world if they can agree together and as a result of the week's work such agreement will be possible. It was clear that the Americans decided to regard us once more as their principle partner in world affairs, and not just as a member of the European queue. (34)

It appeared that the British had succeeded where they had failed in the Summer of 1947. Finally ^{annahme} embracing international Keynesianism the United States had been persuaded to undertake the full obligations of a creditor country on the basis of

policies which would underwrite sterling's world role. Not only London but now Washington seemed to feel that the Marshall Plan was an inadequate response to the dollar shortage. If the wider solution based on Anglo-American economic co-operation apparently heralded by the Washington talks was to be pursued, the United States would cease pressing Britain to participate in schemes to further European integration which jeopardised her reserves.

The impact of the talks on British policy towards Europe was considerable. The improvement in Anglo-American relations took place at a time when relations between Britain and some of her partners in the O.E.E.C. had deteriorated. The British complained bitterly over the size of the O.E.E.C.'s allocation to them of Marshall aid for 1949-50. Alarmed by the dollar drain they revised their estimate of the sterling area dollar deficit for 1949-50 upwards from \$950 million to \$1,500 million. But the Programmes Committee appeared willing to allocate Britain just \$850 million. When other participating countries put in bids which had also been revised upwards (though not as dramatically as the British bid) as the dollar gap widened, it seemed that the O.E.E.C. might be unable to agree on the division of aid. In the end only threats by Paul Hoffman about the consequences of continued disagreement on Congressional and public opinion in the United States brought the dispute to a close. Britain reluctantly accepted a compromise by which she received \$962 million. (35)

The British economic crisis was therefore a major cause of the summer's problems within the O.E.E.C. London's stance on the Intra-European Payments Scheme and on the division of aid, together with the prospect of Anglo-American economic talks in September, worried some participating countries. The French, who relied on the British alliance as the principle counterweight

to resurgent German power, were particularly concerned. They tried unsuccessfully to become associated with the Washington talks. (36)

Following the devaluation of sterling on 18 September the French accused Britain of undermining European integration by settling matters central to the economic stability of O.E.E.C. members in secret session with the Americans. (37)

Confronted with growing evidence of Anglo-American rather than Anglo-European co-operation France joined the participating countries most committed to integration by devising a scheme from which Britain would be excluded. The countries most involved were France, Belgium and Italy. The scheme, known by the British as the 'Alphand Plan', included interconvertibility of members' currencies, fluctuating exchange rates to provide for automatic adjustments to disequilibria, and preferential trading arrangements. E.C.A. strongly supported the plan, seeing in it the core of a European union.

The emergence of the Alphand Plan was clear evidence that the British policy of controlling the pace of European integration through the O.E.E.C. was beginning to ^{schwanen} falter. But the sterling devaluation upset the currency plans of France, Belgium and Italy. As American policy-makers had anticipated in the spring most participating countries were left with little choice but to devalue their own currencies in response to the sterling-dollar readjustment. Progress with the Alphand Plan had to wait upon this wider readjustment. The British were relieved at the apparent demise of the Alphand Plan. They feared first that the Plan's implementation would lead to the appearance of disorderly cross rates and encourage speculation against sterling and secondly that it heralded their exclusion from a protected European market. (38)

Encouraged by the Washington talks and by the emergence of what appeared to be an anti-British conspiracy in Marshall Europe the Labour Government elaborated the 'limited liability' policy developed in January 1949.⁽³⁹⁾ 'Limited liability' meant making no irreversible commitment to European integration. In October 1949 Bevin argued that Britain should specifically work against the development of a European bloc separate from the United States. Such a grouping would be strategically vulnerable to Soviet pressure. Nothing should be done to undermine the pivotal position of the Atlantic Pact in holding the West together and in committing the United States to European defence. Britain should therefore encourage the development of a Western association within which she would lean more towards the United States and the Commonwealth than towards integration with Europe. On 27 October Bevin informed the Cabinet that

as a result of the Washington talks and of the Commonwealth Finance Minister's meeting, we have established or are establishing a new relationship with the United States and with the rest of the Commonwealth (sic). Our relations with those areas take priority over our relations with Europe and for that reason alone there is a limit to the part we can play in 'European Union'.⁽⁴⁰⁾

The Atlanticist shape of British foreign policy had two basic supports. Strategy and economics went hand in hand. The Anglo-American military and political alliance, deemed central to Western security, was paralleled by the understanding between the sterling and dollar areas which removed Britain from the Marshall queue.

Such was the view from London. In Washington the State Department had finally accepted that Britain's world economic role would prevent her from participating fully in European integration. Dean Acheson argued that France now held the key to European unity, which could only be achieved on the basis of a Franco-German rapprochement.⁽⁴¹⁾ Acheson did however believe that Britain should not merely give sympathetic consideration to schemes for European integration. Rather, London should positively encourage the creation of a West European community even if Britain was to be no more than an associate member.⁽⁴²⁾

VI

The new American policy faced the British with the dilemma they had been trying to escape ever since Bevin's Western Union speech in January 1948. Abstention from European Union might lead to the emergence of a protected, powerful industrial competitor. Involvement would prejudice British control over their own financial and economic policies. That much had been made clear by the wrangles over the Intra-European Payments Schemes. The point was driven home in the first months of 1950 by the long and difficult negotiations designed to establish the European Payments Union. In early 1950, therefore, the British launched the concept of an Atlantic Community. The Atlantic Community was the logical development of Bevin's Western Union policy. All the countries of Marshall Europe could be brought under the umbrella of a North Atlantic Treaty Organisation whose function would be extended from the military into the economic sphere. French fears of a revived Germany would be reassured by the presence of Britain and America in the Organisation, which would not involve Britain in a closely integrated Europe. At the same time the Atlantic Community would develop the new sterling-dollar relationship achieved at Washington in September 1949. The health of the sterling area was to be central to the well-being of the Community as a whole. By endorsing the Atlantic Community the United States would be completely committed to supporting Britain's world economic role.⁽⁴³⁾ And the United States, alarmed by the loss of momentum in European integration revealed early in 1950 by the slow progress of the Payments Union talks and by the development of Franco-German antagonism, gradually moved in April 1950 towards an endorsement of the Atlantic Community.

But the Atlantic Community could not accommodate the interests of several leading Marshall countries committed to European integration. France, Italy and Benelux had never been satisfied by Britain's wide and loose concept of Western co-operation. Furthermore the Atlantic Community offered only a slow and clumsy solution to the Franco-German problem. The Schuman Plan, however, cut through these complications. It answered the needs both of the State Department and of the most committed European countries. Washington abandoned the Atlantic Community and the British were faced with the irreversible commitment to European integration they had decided never to make. The Schuman Plan clearly heralded the two-tier development of Western Europe over the subsequent generation, in the E.E.C. under a Franco-German leadership and in N.A.T.O. along an Anglo-American axis.

The Marshall Plan might have provided a framework for European integration but it did not lead to the closing of the dollar gap. In 1947 the American surplus with the rest of the world had been \$8 billion; in 1949 it remained above \$4 billion. Acheson asked President Truman in February 1950

as E.R.P. is reduced and after its termination in 1952, how can Europe and other areas of the world obtain the dollars necessary to pay for a high level of United States exports, which is essential both to their own basic needs and to the well-being of the United States economy? (44)

At the start of 1950 one-third of America's exports of \$16 billion were financed through foreign assistance. On the termination of this assistance the problems of 1947 would reappear.

The Marshall Plan, as the 1949 crisis showed, merely created the conditions for the establishment of an autarkic Western Europe. British criticisms of the Plan were largely justified. Yet the pursuit of multilateralism through sterling-dollar co-operation was effectively abandoned with the onset of the Korean War.

In 1950 and after, however, the United States did pump dollars into the underdeveloped nations of the Far East. The rearmament programme, given a powerful impetus by the Korean War, set off a return to triangular trade. The United States' enthusiastic performance as world policeman finally closed the dollar gap and stimulated international economic expansion. Economic equilibrium was founded upon political disorder: hot war followed by cold war saved the West for capitalism.

- (1) See for example Jean Monnet, Memoirs (1979) and Richard Mayne, The Recovery of Europe (1970), passim; Walter Laqueur, Europe Since Hitler (1970), pp. 102-03; F.S. Northege, Descent from Power (1974), p. 142; and Ernst van der Beugel, From Marshall Aid to Atlantic Partnership (New York, 1966), passim.
- (2) Robert Triffin, The World Money Maze (New Haven, 1966), p. 400.
- (3) Foreign Relations of the United States, 1947, Volume III (hereafter FRUS) pp. 276-83. Summary of a meeting on 25 June 1947.
- (4) See Alan S. Milward, War, Economy and Society 1939-1945 (1977), p. 355.
- (5) PRO T 229/136, memorandum by R. W. B. Clarke, 15 July 1947. See also C.C.S. Newton, 'The Sterling Crisis of 1947 and the British Response to the Marshall Plan', forthcoming in the Economic History Review.
- (6) Organisation for European Economic Co-operation.
- (7) See C.C.S. Newton, 'Britain, the Dollar Shortage, and European Integration, 1945-1950', unpublished Ph.D thesis, University of Birmingham, Chapter VI.
- (8) E.C.A., Recovery Guides, No. 9, June 1949, p. 4.
- (9) Robert Aaron Gordon, Business Fluctuations (New York, 1964), pp. 477-8.
- (10) Ibid., p. 478.
- (11) United Nations, Economic Commission for Europe (hereafter UN,ECE), Economic Survey of Europe in 1949 (Geneva, 1950), p. 143.
- (12) E.C.A. Recovery Guides, No. 10, September 1949, p. 4.
- (13) Elliot Zupnick, Britain's Postwar Dollar Problem (New York, 1957), p. 111.
- (14) The Economist, 3 September 1949, pp. 515-7, 'The Sterling Balances'.

- (15) U.N., E.C.E., Economic Survey of Europe in 1949, p. 134.
- (16) E.C.A., The Sterling Area: An American Analysis (Washington, 1951), pp. 638-9.
- (17) FRUS, 1949, III, p. 377, Hoffman to Harriman, 17 March 1949.
Ibid.
- (18) Ibid., and see FRUS, 949, III, p.379, James Webb (Acting Secretary of State) to Lewis Douglas (United States Ambassador in London), 28 May 1949.
- (19) See for example PRO FO 371/25577, UE 2133/150/53, Sir Stafford Cripps to Sir Oliver Franks, 6 April 1949.
- (20) See C.C.S. Newton, 'Britain, the Dollar Shortage, and European Integration'., p. 255.
- (21) Joyce and Gabriel Kolko, The Limits of Power (New York, 1972), p. 464.
- (22) PRO CAB 129/37, C.P. (49) 228, 'Economic Report',
4 November 1949.
- (23) For a more detailed discussion of American attempts to liberalise European payments arrangements in 1949 see C.C.S. Newton, 'Britain, the Dollar Shortage, and European Integration', pp. 248-59.
- (24) Philip Williams, Hugh Gaitskell (1979), p. 195.
- (25) PRO FO 371/75578, UE 3830/150/53, Minute by R.W.B. Clarke,
16 June 1949.
- (26) PRO CAB 134/220, E.P.C. (49) 27th Meeting, 7 July 1949.
- (27) PRO CAB 134/222, E.P.C. (49) 73, Memorandum by Cripps,
7 July 1949.
- (28) For records of the Cripps-Snyder meetings see PRO FO 371/7559,
passim.

- (29) FRUS 1949, III, pp. 801-2, Snyder to Acheson, 10 July 1949.
- (30) Douglas Jay, Change and Fortune (1980), p. 186.
- (31) PRO CAB 128/16, C.M. (49) 48th Conclusions, 28 July 1949.
- (32) Alonzo L. Hamby, Beyond the New Deal: Harry S. Truman and American Liberalism (New York, 1973), pp. 331-2.
- (33) PRO FO 371/75590, UE 5984/150/53, Franks to Bevin, 19 September 1949.
- (34) See C.C.S. Newton, 'Britain, the Dollar Shortage, and European Integration', pp. 275-7.
- (35) PRO FO 371/75586, UE 5578/150/53, minute by Sir Roger Makins to Bevin, 29 August, 1949.
- (36) David McLellan, Dean Acheson, The State Department Years (New York, 1976), p. 242.
- (37) On cross rates see PRO FO 371/75590, UE 5980/150/53, minute by K.R.C. Pridham, 21 September 1949; on exclusion see PRO FO 371/78103, UE 10095/306/98, letter from Eric Berthoin to Roger Makins, 1 October 1949.
- (39) See PRO CAB 134/221, E.P.C. (49) 6, 25 January 1949.
- (40) PRO CAB 129/37, CP (49) 203, joint memorandum by Bevin and Cripps, 'Proposals for the Economic Unification of Europe'.
- (41) See C.C.S. Newton, 'Britain, the Dollar Shortage, and European Integration, 1945-1950', pp. 284-6.
- (42) PRO FO 371/78104, UR 11088/306/98, Acheson to Bevin, 25 October 1949.
- (43) See C.C.S. Newton, 'Britain, the Dollar Shortage, and European Integration', 1945-1950', pp. 316-7.
- (44) FRUS, 1950, I, pp. 834-5, Acheson to Truman, 16 February 1950.

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